

Credit Opinion

7 November 2024

Ratings

Senior Unsecured Debt Rating	BBB _g -
Long-Term Credit Rating	BBB _g -
Outlook	Stable
Category	Corporate
Domicile	China
Rating Type	Solicited Rating

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Anhui Zhoulai Holdings (Group) Co., Ltd.

Initial credit rating report

CCXAP assigns first-time long-term credit rating of BBB_g- to Anhui Zhoulai Holdings (Group) Co., Ltd., with stable outlook.

Summary

The BBB_g- long-term credit rating of Anhui Zhoulai Holding (Group) Co., Ltd. ("AZHG" or the "Company") reflects (1) Fengtai County Government's relatively strong capacity to provide support, and (2) the local government's extremely high willingness to provide support, based on our assessment of the Company's characteristics.

Our assessment of Fengtai County Government's capacity to support reflects its economic importance in Huainan City, with ongoing economic and fiscal growth, but is constrained by its small economic and fiscal scale.

The rating also reflects the local government's willingness to support, which is based on the Company's (1) important role in infrastructure construction of Fengtai County; and (2) good track record of receiving ongoing government support.

However, the rating is constrained by the Company's (1) medium exposure to commercial activities; (2) increasing debt burden; and (3) moderate asset liquidity.

The stable outlook on AZHG's rating reflects our expectation that the local government's capacity to support will remain stable, and the Company will maintain its important role in the development of Fengtai County.

Rating Drivers

- Important role in infrastructure construction of Fengtai County
- Medium exposure to commercial activities
- Good track record of receiving ongoing government support
- Increasing debt burden but with reasonable debt structure
- Moderate asset liquidity
- Low reliance on non-standard financing

Rating Sensitivities

What could upgrade the rating?

The rating could be upgraded if (1) the local government's capacity to support strengthens; and (2) the Company's characteristics change in a way that strengthens the local government's willingness to support, such as decrease in exposure to commercial activities or improvement in debt burden.

What could downgrade the rating?

The rating could be downgraded if (1) the local government's capacity to support weakens; or (2) the Company's characteristics change in a way that weakens the local government's willingness to support, such as decrease in its strategic significance; decrease in government payments; or increase in debt burden.

Key Indicators

	2021FY	2022FY	2023FY
Total Asset (RMB billion)	4.6	14.8	26.5
Total Equity (RMB billion)	3.2	7.5	12.2
Total Revenue (RMB billion)	0.2	0.5	0.8
Total Debt/Total Capital (%)	26.7	47.6	52.2

All ratios and figures are calculated using CCXAP's adjustments.
Source: Company data, CCXAP research

Corporate Profile

Established in 2016, AZHG is an important local infrastructure investment and financing company ("LIIFC") in Fengtai County. The Company primarily focuses on urban development activities including water environmental management and shantytown renovation. It is also involved in other commercial activities such as trading and leasing. AZHG is ultimately controlled and 100% owned by the Fengtai County State-owned Assets Supervision and Administration Commission.

Exhibit 1. Revenue structure in 2023

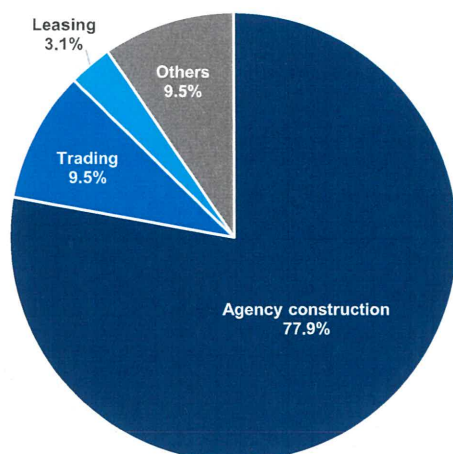
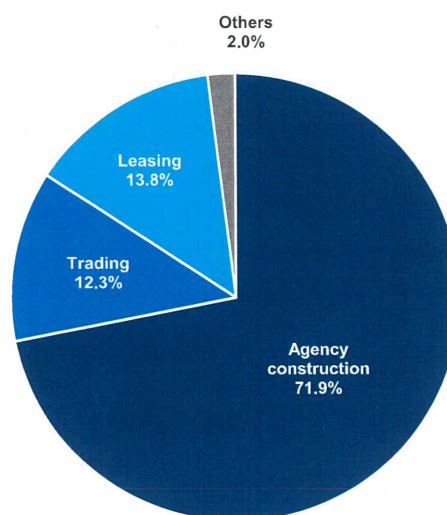


Exhibit 2. Gross Profit Structure in 2023



Source: Company information, CCXAP research

Rating Considerations

Government Capacity to Support

We believe the Fengtai County Government has a strong capacity to provide support to the Company, given its economic importance in Huainan City, with ongoing economic and fiscal growth.

Located in the north-central part of Anhui Province, Huainan City is one of the integrated regional cities in the Yangtze River Delta. It has formed pillar industries including coal, chemicals, electricity and pharmaceuticals. Huainan City's economy has demonstrated a growth trend over the past years. Benefiting from the ongoing development of its pillar industries, Huainan City's GRP increased from RMB145.7 billion in 2021 to RMB160.2 billion in 2023, ranking 12th among prefecture-level cities in Anhui Province. With ongoing economic growth, the general budgetary revenue of Huainan City also increased from RMB11.0 billion in 2021 to RMB13.1 billion in 2023. It has moderate fiscal stability, with tax income accounting for around 66.7% of the general budgetary revenue over the past three years. As the end of 2023, the outstanding direct government debt balance of Huainan Municipal Government amounted to RMB59.1 billion, accounting for 36.9% of its GRP. In 2024H1, Huainan City has achieved GRP of RMB82.8 billion, with a YoY growth rate of 4.5%.

Exhibit 3. Key Economic and Fiscal Indicators of Huainan City

	2021FY	2022FY	2023FY
GRP (RMB billion)	145.7	154.1	160.2
GRP Growth (%)	5.7	2.0	5.1
General Budgetary Revenue (RMB billion)	11.0	12.0	13.1
General Budgetary Expenditure (RMB billion)	27.8	29.9	31.6
Local Government Debt (RMB billion)	37.5	42.1	59.1

Source: Statistic Bureau of Huainan City, CCXAP research

Located in the middle reaches of the Huai River, Fengtai County is a county of Huainan City with a total area of 1,095.6 square kilometers. Fengtai County relies on coal and electricity as its pillar industries and is the largest county for deep coal mining. It has stable economic growth in recent years. From 2021 to 2023, Fengtai County's GRP increased from RMB34.0 billion to RMB35.6 billion, ranking 2nd among all counties and districts in Huainan City.

With the ongoing development of the regional economy, Fengtai County's fiscal income has also increased. From 2021 to 2023, its general budgetary revenue increased from RMB2.2 billion to RMB3.1 billion. It also has good fiscal stability with tax income contributing to over 80% of the general budgetary revenue over the past three years. It has a moderate fiscal balance ratio (general budgetary revenue/general budgetary expenditure) of 63.6% over the past three years. In 2023, Fengtai County had an outstanding direct government debt balance of RMB7.4 billion, accounting for 20.7% of its GRP. In 2024H1, Fengtai County has achieved GRP of RMB21.3 billion, with a YoY growth rate of 5.7%.

Exhibit 4. Key Economic and Fiscal Indicators of Fengtai County

	2021FY	2022FY	2023FY
GRP (RMB billion)	34.0	34.8	35.6
GRP Growth (%)	5.3	-0.9	3.7
General Budgetary Revenue (RMB billion)	2.2	2.9	3.1
General Budgetary Expenditure (RMB billion)	3.7	4.4	4.7
Local Government Debt (RMB billion)	4.7	6.0	7.4

Source: Statistic Bureau of Fengtai County, CCXAP research

Government Willingness to Support

Important role in infrastructure construction of Fengtai County

There are two main urban development and operation entities in Fengtai County, namely Fengtai Huaxing City Construction Investment Co., Ltd. ("FHCI") and AZHG. FHCI is mainly responsible for infrastructure construction in Fengtai County. As an important urban developer in Fengtai County, AZHG has undertaken a large amount of integrated environmental governance projects, shantytown renovation, and new energy projects in Fengtai County, making great contributions to the urbanization of the region. Considering its strategic significance to the development of Fengtai County, we believe the Company is unlikely to be replaced by other local state-owned enterprises in the foreseeable future.

Entrusted by Fengtai County Fengyin Drinking Water Project Investment Construction Co., Ltd. and the Fengtai County Government, the Company undertakes infrastructure construction projects under agent construction model. Upon construction completion, the local government will make payments to the Company in instalments at a price equal to the investment costs plus a 25% markup. As of 31 December 2023, the Company had 10 infrastructure construction projects under construction, with a total planned investment of around RMB10.2 billion and uninvested amount of around RMB7.6 billion, indicating high capital expenditure pressure. The Company also has 4 infrastructure construction projects under planning, with a total planned investment of RMB4.2 billion.

Medium exposure to commercial activities

AZHG's commercial businesses mainly include property leasing and trading business. We consider the Company's exposure to commercial businesses to be medium, accounting for around 30% of its total assets. The Company has diversified into sandstone mining and photovoltaic power generation businesses, with

estimated investment of RMB3.2 billion, which are expected to increase its capital expenditure pressure and commercial exposure.

The Company engages in property leasing business. Its rental properties mainly include office buildings, factory buildings, stadiums and commercial properties. As of 31 December 2023, the Company owned 257 properties with a total leasable area of 77.2 thousand square meters and a total assessed value of RMB455.5 million. It has received rental income of RMB24.0 million in 2023, contributing 3.1% of total revenue to the Company. In addition, the Company leases out self-owned forest with area of 49.5 thousand mu and receives RMB9.9 million every year.

The Company also participated in trading business. Its commodity trading business mainly includes agricultural and photovoltaic products. In addition, its top five customers and upstream suppliers are mainly photovoltaic equipment companies, which may expose the Company to concentration risk. This business only accounts for 9.5% of the Company's total revenue.

Good track record of receiving ongoing government support

As an important urban development and operation entity in Fengtai County, the Company has a proven history of receiving support from Fengtai County government through various channels including asset injection, capital injections and subsidies. In 2022, the Company totally received capital injections of RMB1.0 billion from the Fengtai County Finance Bureau. From 2021 to 2023, it also received subsidies of RMB68.1 million in total from the local government. In the meantime, the local government had transferred operation rights for sandstone mining projects and shares in a state-owned enterprise to the Company, significantly enhancing its capital strength. Given its important position in the development of Fengtai County, we believe that the Fengtai County government will continue to provide support to the Company.

Increasing debt burden but with reasonable debt structure

With the increasing financing demand for the construction projects, AZHG has a fast debt growth over the past three years. The Company's total debt increased from RMB1.2 billion at end-2021 to RMB13.3 billion at end-2023, with a total capitalization ratio of 52.2%. In addition, the Company has a reasonable debt structure and manageable short-term debt level. As of 31 December 2023, its short-term debts accounted for about 9.0% of total debt and cash to short-term debt ratio was 1.2x, indicating adequate cash flow to service its short-term debts. With pipeline of infrastructure construction projects under construction, the Company will continue to rely on external financing to meet its future capital expenditure needs. Thus, we expect that its debt burden will continue to grow in the next 12 to 18 months.

The Company has manageable contingent liabilities risk. As of 31 December 2023, the Company recorded an external guarantee amount of RMB2.1 billion, accounting for about 17% of its total equity. Those guaranteed entities are the local state-owned enterprises in Fengtai County. The credit risk of the Company might be heightened if one of the guaranteed entities suffers from credit issues.

Moderate asset liquidity

AZHG has moderate asset liquidity, which may undermine its financing flexibility. As of 31 December 2023, the Company's total assets mainly consist of intangible assets, inventories, and receivables, with low liquidity, accounting for around 66% of total assets. The Company's intangible assets mostly contained sand and gravel mining and operating rights. Inventories were primarily the project development costs and land use rights, while

the receivables mainly composed uncollected payments from the local government department and state-owned enterprises.

Low reliance on non-standard financing

AZHG mainly relies on bank loans for funding. As of 31 December 2023, bank loans accounted for 90.5% of the Company's total debt, with an average interest rate of around 4.7%. It maintains a good relationship with several policy banks and commercial banks, such as China Development Bank and Rural Commercial Bank. As of 31 December 2023, it had available credit facilities of about RMB4.2 billion. Besides, it has a relatively low reliance on non-standard financing, accounting for around 10% of total debt. In addition, the Company has not issued bonds in the public market and plans to tap the bond markets to broaden its funding channels.

ESG Considerations

AZHG assumes environmental risks through its urban infrastructure projects. Such risks could be moderated through environmental studies and detailed planning prior to the start of the projects and close supervision during construction.

In terms of social awareness, AZHG has played a crucial role in the social welfare of Fengtai County by involving the construction of public projects and shantytown projects in Fengtai County.

In terms of corporate governance, AZHG's governance considerations are also material as the Company is subject to local government oversight and reporting requirements, reflecting its public-policy role and status as a government-owned entity.

Structural Consideration

AZHG's senior unsecured debt rating is equivalent to its long-term credit rating. We believe that government support will flow through the Company given its important position in the development of Fengtai County, thereby mitigating any differences in an expected loss that could result from structural subordination.

Rating Methodology

The methodology used in this rating is the Rating Methodology for [China's Local Infrastructure Investment and Financing Companies \(July 2022\)](#).

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